

Report of the auditor-general to the Limpopo provincial legislature and the council on Mopani District Municipality

Report on the financial statements

Introduction

1. I was engaged to audit the financial statements of the Mopani District Municipality set out on pages ... to ..., which comprise the statement of financial position as at 30 June 2015, the statement of financial performance, statement of changes in net assets, and cash flow statement and statement of comparison of budget information with actual information for the year then ended, as well as the notes, comprising a summary of significant accounting policies and other explanatory information.

Accounting officer's responsibility for the financial statements

2. The accounting officer is responsible for the preparation and fair presentation of these financial statements in accordance with the South African Standards of Generally Recognised Accounting Practice (SA Standards of GRAP) and the requirements of the Municipal Finance Management Act of South Africa, 2003 (Act No. 56 of 2003) (MFMA) and the Division of Revenue Act, 2014 (Act No. 10 of 2014) (DoRA), and for such internal control as the accounting officer determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

Auditor-general's responsibility

3. My responsibility is to express an opinion on the financial statements based on conducting the audit in accordance with International Standards on Auditing. Because of the matters described in the basis for disclaimer of opinion paragraphs, however, I was unable to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion.

Basis for disclaimer of opinion

Consumer debtors

4. I was unable to obtain sufficient appropriate audit evidence for consumer debtors relating to water and sewerage transactions included in note 9 to the financial statements due to inadequate internal control and accounting systems. I was unable to determine if water and sewerage transactions are recorded at correct amounts as the municipality's records did not permit the application of alternative audit procedures. Consequently, I was unable to determine whether any adjustment relating to this consumer debtors stated at R298 578 682 (2014: R230 182 355) in the financial statements was necessary.

5. The municipality did not assess consumer debtors for impairment individually for significant financial assets or collectively for insignificant financial assets in accordance with SA Standards of GRAP 104, *Financial instruments*. I was unable to determine the amount of impairment by alternative means as the municipality did not maintain adequate records. Consequently, I was unable to determine whether any adjustments to the provision for doubtful debt balance amounting to R276 873 330 (2014: R255 913 555) as disclosed in note 9 to the financial statements was necessary.

Receivables from exchange transactions

6. I was unable to obtain sufficient appropriate audit evidence for receivables from exchange transactions relating to water and sewerage transactions included in note 7 to the financial statements due to inadequate internal controls and accounting systems. I was unable to determine if water and sewerage transactions are recorded at correct amounts as the municipality's records did not permit the application of alternative audit procedures regarding the receivable amounts from the local municipalities within its jurisdiction. Consequently, I was unable to determine whether any adjustment relating to this receivables stated at R338 752 968 (2014: R289 211 713) in the financial statements was necessary.

Revenue

7. The municipality did not have an adequate system of internal control to record all revenue from service charges. This resulted in revenue from service charges being understated by R44.3 million. In addition, I was unable to obtain sufficient appropriate audit evidence that all revenue from service charges has been recorded by alternative means. Consequently, I was unable to determine whether any further adjustments to revenue from service charges stated at R158 809 610 (2014: R134 866 082) in note 16 to the financial statements were necessary.
8. The municipality did not have an adequate system of internal control to record all revenue on interest from outstanding debtors relating to water and sewerage included in note 16 to the financial statements. I was unable to obtain sufficient appropriate audit evidence that all interest revenue from outstanding debtors relating water and sewerage has been recorded by alternative means. Consequently, I was unable to determine whether any adjustment to interest revenue relating to outstanding debtors and consumer debtors from water and sewerage stated at R15 905 432 (2014: R13 778 874) and R298 578 682 (2014: R 230 182 355) respectively in the financial statements was necessary.

Property plant and equipment

9. I identified a number of infrastructure assets belonging to the municipality that were not accounted for in the underlying records. In the absence of an adequate internal control system over the recording of infrastructure assets, I was not able to determine whether any adjustment to property plant and equipment of R4 301 420 828 (2014: R4 371 895 876) disclosed in note 3 to the financial statements was necessary.
10. The municipality did not have a system of control over property, plant and equipment as assets amounting to R165 252 803 that do not belong to the municipality, were recognised in the accounting records. Consequently, property plant and equipment was overstated by R165 252 803. Additionally, there was a resultant impact on surplus for the period and on the accumulated surplus.

11. The municipality did not adequately assess impairment of property, plant and equipment in accordance with the SA standards of GRAP 21, *Impairment of assets*. I identified assets amounting to R15 708 644 with impairment indicators which were not impaired by the municipality. I was not able to determine the impact on the net carrying amount of property, plant and equipment, as it was impracticable to do so.
12. The municipality did not perform an assessment on useful life for all assets where there was an indication of change in estimate accordance with the SA Standards of GRAP 17, *Property, plant and equipment* and GRAP 3, *Change in estimate in useful of assets*. Consequently, I was unable to determine whether any depreciation adjustments to the property, plant and equipment balance of R4 505 017 113 (2014: R4 583 262 990) as per note 3 to the financial statements were necessary.
13. The municipality did not recognise infrastructure assets in accordance with SA Standards of GRAP 17, *Property, plant and equipment*. Completed capital projects to the value of R98.2 million were not broken up according to component as required by GRAP17. Furthermore I identified unexplained differences amounting to R33 347 357 between the municipality's accounting records and my calculations. As the municipality did not maintain adequate systems for recording assets, I was unable to confirm these amounts by alternative means. Consequently, I was unable to determine whether any adjustments to the property, plant and equipment, depreciation for the period and accumulated surplus were necessary.

Inventory

14. I identified water inventory (consumables and physical water) belonging to the municipality that was not included in the accounting records. In the absence of an adequate internal control system over the recording of water inventory, I was not able to determine the extent of the understatement for inventory balance stated at R15 548 740 (2014: R34 884 613) as disclosed in note 6 to the financial statements.

Consumer deposits

15. I was unable to obtain sufficient appropriate audit evidence that consumer deposits had been properly accounted for, as the municipality did not maintain an adequate system of internal control. I was unable to confirm consumer deposits by alternative means. Consequently, I was unable to determine whether any adjustment to consumer deposits stated at R4 385 240 (2014: R3 349 635) in note 15 to the financial statements was necessary.

Expenditure

16. During 2013-14, I was unable to obtain sufficient appropriate audit evidence to adjusting journal entries amounting to R11 855 914. These journals could not be substantiated by supporting audit evidence. I was unable to confirm the journals by alternative means. Consequently, I was unable to determine whether any adjustments the expenditure account stated at R832 326 885 (2014: R1 164 295 573) in the financial statements was necessary.

Debt impairment

17. The municipality did not completely record expenses relating to debt impairment in the surplus for the period. This resulted in an understatement of the provision for debt impairment in surplus for the period stated at R2 776 708 (2014: R36 096 254) and an understatement of consumer debtors stated at R 298 578 682 (2014: R 230 182 355) respectively in the financial statements.

Irregular expenditure

18. The municipality did not include particulars of irregular expenditure in note 39 to the financial statements. The municipality made payments in contravention of the supply chain management requirements which were not included in the note on irregular expenditure, resulting in irregular expenditure being understated by R2 140 162 (2014: R6 085 634). Due to lack of a proper system of internal control to account and report irregular expenditure I was unable to confirm that all amounts relating to irregular expenditure in the current year has been recorded. Consequently, I am unable to determine if any adjustments to irregular expenditure stated at R174 794 070 (2014: R174 794 070) were necessary.

Commitments

19. I identified commitments to the amount of R101 465 174 that belong to the municipality which were not included in the accounting records. In the absence of an adequate internal control system over the recording of commitments, I was not able to determine the extent of the understatement in the commitments' balance of R433 303 568 (2014: R106 262 010) as disclosed in note 33 to the financial statements.

Cash flow statement

20. The municipality did not apply the principles of the SA Standards of GRAP 2 *Cash flow statements* as non-cash flow items were not excluded in the calculation. I was unable to determine the correct movement on cash flow from operations as it was impractical to do so. Consequently, I was unable to determine the impact on the cash flow balance stated at R114 326 793 (2014: R83 126 281) in the cash flow statement.

Distribution losses

21. I was unable to obtain sufficient appropriate audit evidence for distribution losses relating to water losses, included in note 43 of the financial statements due to inadequate internal controls and accounting system. I was unable to determine if water losses are recorded at correct amounts as the municipality's records did not permit the application of alternative audit procedures. Consequently, I was unable to determine whether any adjustment relating to distribution losses in the financial statements was necessary.

Opinion

22. Because of the significance of the matters described in the basis for disclaimer of opinion paragraphs, I have not been able to obtain sufficient appropriate audit evidence to provide a basis for an audit opinion. Accordingly, I do not express an opinion on the financial statements.

Emphasis of matters

23. I draw attention to the matters below. My opinion is not modified in respect of these matters.

Unauthorised expenditure

24. As disclosed in note 37 to the financial statements, unauthorised expenditure to the amount of R1 038 038 was incurred as a result of overspending of the vote.

Significant uncertainties

25. With reference to note 34 to the financial statements the municipality is the defendant in various lawsuits. The ultimate outcome of the matter cannot presently be determined and no provision for any liability that may result has been made in the financial statements.

Restatement of corresponding figures

26. As disclosed in note 36 to the financial statements, the corresponding figures for 30 June 2014 have been restated as a result of an error discovered during 2015 in the financial statements of Mopani District Municipality at, and for the year ended, 30 June 2014.

Financial sustainability

27. The statement of financial position indicates that the municipality's current liabilities exceeded its total current assets by R218 767 508 which may indicate the existence of a material uncertainty that may cast significant doubt on the municipality's ability to operate as a going concern. It affects the municipality's ability to meet its short term commitments and thus negatively impacting service delivery.

Additional matters

28. I draw attention to the matters below. My opinion is not modified in respect of these matters.

Withdrawal from the audit engagement

29. Due to the limitation imposed on the scope of the audit by management, I have disclaimed my opinion on the financial statements. But for the legislated requirement to perform the audit of municipality, I would have withdrawn from the engagement in terms of the ISAs

Unaudited supplementary schedules

30. The supplementary information set out on pages xx to xx does not form part of the financial statements and is presented as additional information. I have not audited these schedules and, accordingly, I do not express an opinion thereon.

Unaudited disclosure notes

31. In terms of section 125(2)(e) of the MFMA the municipality is required to disclose particulars of non-compliance with the MFMA. This disclosure requirement did not form part of the audit of the financial statements and accordingly I do not express an opinion thereon.

Report on other legal and regulatory requirements

32. In accordance with the Public Audit Act of South Africa, 2004 (Act No. 25 of 2004) (PAA) and the general notice issued in terms thereof, I have a responsibility to report findings on the reported performance information against predetermined objectives for selected development priorities presented in the annual performance report, compliance with legislation and internal control. The objective of my tests was to identify reportable findings as described under each subheading, but not to gather evidence to express assurance on these matters. Accordingly, I do not express an opinion or conclusion on these matters.

Predetermined objectives

33. I performed procedures to obtain evidence about the usefulness and reliability of the reported performance information for the following selected development priorities presented in the annual performance report of the municipality for the year ended 30 June 2015:
- Development priority 3: Develop and maintain infrastructure on pages xx to xx
 - Development priority 4: Provide clean and safe water on pages xx to xx
34. I evaluated the reported performance information against the overall criteria of usefulness and reliability.
35. I evaluated the usefulness of the reported performance information to determine whether it was presented in accordance with the National Treasury's annual reporting principles and whether the reported performance was consistent with the planned development priorities. I further performed tests to determine whether indicators and targets were well defined, verifiable, specific, measurable, time bound and relevant, as required by the National Treasury's *Framework for managing programme performance information* (FMPPI).
36. I assessed the reliability of the reported performance information to determine whether it was valid, accurate and complete.
37. The material findings in respect of the selected development priorities are as follows:

Usefulness of reported performance information

38. I did not identify material findings on the usefulness of the reported performance information for the following development priority:

- Develop and maintain infrastructure
- Provide clean and safe water

Reliability of reported performance information

Develop and maintain infrastructure

39. The FMPPPI requires auditees to have appropriate systems to collect, collate, verify and store performance information to ensure valid, accurate and complete reporting of actual achievements against planned objectives, indicators and targets. I was unable to obtain the information and explanations I considered necessary to satisfy myself as to the reliability of the reported performance information for the following development priorities:

- Develop and maintain infrastructure
- Provide clean and safe water

This is due to the fact that the auditee could not provide sufficient appropriate evidence in support of the reported performance information.

Additional matters

40. I draw attention to the following matters:

Achievement of planned targets

41. Refer to the annual performance report on pages xx to xx; for information on the achievement of planned targets for the year. This information should be considered in the context of material findings on reliability of the reported performance information in paragraphs 39 of this report.

Unaudited supplementary information

42. The supplementary information set out on pages x to x does not form part of the annual performance report and is presented as additional information. We have not audited these schedules and, accordingly, we do not express a conclusion thereon.

Compliance with legislation

43. I performed procedures to obtain evidence that the district municipality had complied with applicable legislation regarding financial matters, financial management and other related matters. My material findings on compliance with specific matters in key legislation, as set out in the general notice issued in terms of the PAA, are as follows:

Annual financial statements, performance and annual reports

44. The financial statements submitted for auditing were not prepared in all material respects in accordance with the requirements of section 122 of the MFMA. Material misstatements of non-current assets, current assets, liabilities, revenue, expenditure, disclosure items identified by the auditors in the submitted financial statements were subsequently corrected and the supporting records were provided subsequently, but the uncorrected material misstatements and supporting records that could not be provided resulted in the financial statements receiving a disclaimer audit opinion.

Audit committee

45. The audit committee did not meet at least four times a year, as required by section 166(4)(b) of the MFMA.

Procurement and contract management

46. Awards were made to providers who are in the service of the municipality and whose principal shareholders are in the service of the municipality in contravention of section 112(j) of the MFMA and *Supply Chain Management regulation* (SCM regulation) 44. Furthermore, the provider failed to declare that he/she was in the service of the municipality, as required by SCM regulation 13(c). Similar non-compliance was reported in the prior year and the municipality did not take disciplinary action against the officials involved.
47. Sufficient appropriate audit evidence could not be obtained that all contracts and were awarded in accordance with the legislative requirements and a procurement process which is fair, equitable, transparent and competitive, as a limitation of scope relating to the forensic investigation were found.
48. Measures to combat the abuse of the SCM system were not implemented as per the requirements of SCM regulation 38(1), because awards were made to providers who: abused the SCM system of the municipality
49. Contracts were awarded to bidders who did not submit a declaration on whether they are employed by the state or connected to any person employed by the state, as required by SCM regulation 13(c).

Expenditure management

50. Money owed by the municipality was not always paid within 30 days, as required by section 65(2)(e) of the MFMA
51. Reasonable steps were not taken to prevent unauthorised, irregular as well as fruitless and wasteful expenditure, as required by section 62(1)(d) of the MFMA

Budget management

52. Expenditure was not incurred in accordance with the approved budget, in contravention of section 15 of the MFMA.

Consequence management

53. Unauthorised, irregular as well as fruitless and wasteful expenditure incurred by the municipality was not investigated to determine if any person is liable for the expenditure, as required by section 32(2)(a)(ii) of the MFMA.

Revenue management

54. An adequate management, accounting and information system which accounts for revenue, debtors and receipts of revenue was not in place, as required by section 64(2)(e) of the MFMA.
55. An effective system of internal control for debtors and revenue was not in place, as required by section 64(2)(f) of the MFMA.
56. Sufficient audit evidence could not be obtained that interest had been charged on all accounts in arrears, as required by section 64(2)(g) of the MFMA.
57. A credit control and debt collection policy was not implemented, as required by section 96(b) of the Municipal Systems Act, 2000 (Act No. 32 of 2000) (MSA) and section 62(1)(f)(iii) of MFMA.

Asset management

58. An adequate management, accounting and information system which accounts for assets was not in place, as required by section 63(2)(a) of the MFMA.
59. An effective system of internal control for assets (including an asset register) was not in place, as required by section 63(2)(c) of the MFMA.

Liability management

60. An effective system of internal control for liabilities (including a liability register) was not in place, as required by section 63(2)(c) of the MFMA.

Internal control

61. I considered internal control relevant to my audit of the financial statements, annual performance report and compliance with legislation. The matters reported below are limited to the significant internal control deficiencies that resulted in the basis for disclaimer of opinion, the findings on the annual performance report and the findings on compliance with legislation included in this report.

Leadership

62. Management did not demonstrate the importance of integrity and ethical values to support the functioning of the system of internal control; hence a forensic investigation was conducted in this regard.

63. Actions plans were developed however, it was not fully implemented, reviewed and monitored during the course of the year and resulting in many repeat findings from the prior year.
64. Management did not exercise adequate and sufficient oversight responsibility over the enforcement and implementation of the GRAP standards in preparation of the financial statements.

Financial and performance management

65. The municipality did not have a proper system of record management that provides for the maintenance of information that supports the financial statements and reported performance information.
66. Management did not always provide the required supervision and review over daily and monthly recording and reconciliation of transactions and account balances to ensure that the municipality complies with will applicable financial reporting.

Governance

67. Those charged with governance did not regularly provide adequate oversight over the effectiveness of the internal control environment, including financial and performance reporting and compliance with laws and regulations.

Other reports

Investigations

68. An independent consulting firm performed an investigation at the request of the municipality, which covered the period 2012-2013 to 2014-2015. The investigation was initiated based on allegations of possible misappropriation of the municipality's assets. The outcome of the investigation was reported on 21 October 2015. Council will decide on any further action to be taken.

Auditor-General

Polokwane

21 December 2015



AUDITOR - GENERAL
SOUTH AFRICA

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